

Special Comment

Moody's U.S. Public Finance

September 2008

Announcement: Moody's to Recalibrate its US Municipal Bond Ratings to the Company's Global Rating Scale

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Beginning in October 2008, Moody's Investors Service will recalibrate its ratings of US municipal bond issues and issuers, and migrate these ratings to its global rating scale. The purpose of this transition is to facilitate comparability of credit quality across Moody's entire rated universe.¹

Over a short period of time, Moody's will transition its US municipal ratings by sector. The transition of ratings for a given sector, other than local governments, will take place on a single day during the transition period.² The process will begin with state government general obligation ratings, immediately followed by general obligation ratings of the 50 largest issuers of local government debt and other closely related entities. Moody's will then transition its ratings of issuers and obligations in the enterprise sectors such as health care, higher education, infrastructure and housing, and then the balance of local government ratings. For other local governments we expect to transition ratings weekly, by state or groups of states.

All bonds of an issuer with a general obligation pledge or related to a general obligation pledge such as those on lease and appropriation bonds will be migrated at the same time. However, bonds with other security pledges such as sales tax or special taxes will be transitioned separately, grouped by state, after all general obligation-backed debt is transitioned. We expect to complete the entire transition by early 2009. (For roll-out order and timing, see Table 1)

¹ Municipal credits that receive formal support and whose ratings are based solely on such support – for example issues supported by insurance, guarantee or letter of credit – from a third party rated on Moody's global scale are already rated on the global scale and will not be subject to any rating transition.

² In some sectors there are types of ratings that have linkages/dependencies to an issuer in another sector (e.g. community college districts, county-owned hospitals, municipal power distributors, etc). These ratings will be migrated at the same time as the rating that they are dependent on – for example a county-owned hospital will be migrated to the global scale along with the local government sector.



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During the transition period, we will assign new ratings that are consistent with the current ratings of other credits in a given sector. For example, if ratings in the airport sector have not yet been recalibrated to the global scale, then new ratings for airport debt will be assigned on the municipal scale. If ratings in the health care sector have been recalibrated to the global scale then new health care ratings will be assigned on the global scale.

Prior to the migration of each sector, Moody's will publish a sector-specific methodology that outlines our analytical approach and factors that are considered in the placement of the sector's ratings on the global scale.

Throughout the transition, Moody's intends that its products and services will clearly identify ratings that have been migrated to the global scale. For example, users of Moodys.com will see a notation attached to the information displayed about an issue that will indicate if a rating has been converted to the global scale. Additionally, to enhance clarity during the transition period Moodys.com will have a new, separate area that will be dedicated to the transition of municipal ratings. This area will include: (i) research related to the transition including sector-specific migration methodologies; (ii) downloadable lists of transitioned ratings by sector; and (iii) a tool that will enable users to search the lists of transitioned ratings – by issuer name or CUSIP – to obtain the global scale rating for an issue and the related municipal scale rating at the time of transition.

Initiating the Transition

To initiate the transition, Moody's will benchmark and recalibrate a number of representative municipal credits to the global scale. This benchmarking exercise will employ rating committees composed of analysts from across Moody's analytical organization, including corporate, sub-sovereign, sovereign, project finance and structured finance teams as well as US municipal bond analysts. The assignment of global scale ratings to these benchmark credits will anchor municipal ratings to the global scale and serve as points of reference for the assignment of other municipal ratings. Existing global scale ratings that have been assigned to municipal debt will also be reviewed in the context of this benchmarking process.

Our preliminary analysis indicates that, on average, state and local government general obligation global scale ratings likely will be 2 notches higher than their current ratings on the municipal scale. Global scale ratings for credits in the enterprise sectors are expected to be about 1 notch higher, on average. Ratings at or above Aa3 are generally likely to receive less upward movement than those rated below Aa3.

Background: Market Developments Prompt Reconsideration of the Public Finance Ratings

Moody's has used a distinct rating scale for US municipal bonds since the early 1900s. The municipal scale reflects the generally lower level of credit risk for municipal obligations as well as the discrete nature of the US tax-exempt bond market, which has historically operated independently in the US debt capital markets with its own investor, issuer and broker-dealer communities. In the late 1990s, as a growing number of "cross-over" investors became active in both the taxable and tax-exempt markets, Moody's began exploring the utility of recalibrating its US municipal bond ratings to the global scale. However, market research conducted between 2001 and early 2007 consistently indicated that market participants – investors and issuers alike – generally were opposed to any such recalibration.

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In early 2008, prompted by recent market events and a shift in market sentiment, Moody's again proposed recalibration of its municipal ratings to the global scale. The comments we received on our recent Request for Comment publications³ and in our outreach efforts show that a substantial portion of the market strongly seeks comparability between municipal ratings and those in other sectors. Feedback from nearly 200 market participants – including issuers, bankers, financial advisors, trade associations and major institutional investors with substantial positions in US municipal bonds indicates that:

- current market conditions have resulted in a greater need for rating comparability between municipal and non-municipal securities; and
- a single rating scale applicable to all such securities is preferable to a dual scale system and will be easier to utilize.

We have decided to undertake this transition to respond to the needs of the market.

Table 1

Migration Timeline	
US Municipal Bond Ratings	
Recalibrated ratings issued by end of:	Sectors/Credits
October 2008	<ul style="list-style-type: none"> ◆ State Governments -- General Obligation (GO) and GO-Related Ratings ◆ 50 Largest Local Government Debt Issuers -- GO and GO-Related Ratings
November 2008	<ul style="list-style-type: none"> ◆ Higher Education ◆ Health Care
December 2008	<ul style="list-style-type: none"> ◆ Housing ◆ Airports ◆ Ports ◆ Toll-Roads ◆ Public Power ◆ Mass-Transit
January 2009	<ul style="list-style-type: none"> ◆ Local Government GO and Related Ratings, Local Government Water/Sewer Enterprise and State and Local Government Sales/Special Tax Ratings and all remaining credits.

Moody's Related Research

Special Comments:

- Announcement: Moody's Extends Comment Period on U.S. Public Finance Rating Scale, June 2008 (109143)
- Request for Comment: Assignment of Global Ratings to Tax Exempt Municipal Obligations, March 2008 (108116)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

³ Assignment of Global Ratings to Tax-Exempt Municipal Obligations, March 2008; Moody's Extends Comment Period on U.S. Public Finance Rating Scale, June 2008

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